





## APPENDIX

### Statutes Involved

**Sections of Chapter X of the Bankruptcy Act (52 Stat. 883; 11 U. S. C. 501 *et seq.*).**

"Sec. 130. Every petition shall state—

. . . . .

"(5) the nature of all pending proceedings affecting the property of the corporation known to the petitioner or petitioners and the courts in which they are pending;

. . . . .

"(7) the specific facts showing the need for relief under this chapter \* \* \*.

"Sec. 131. A creditors' \* \* \* petition shall, in addition to the allegations required by section 130 of this Act, state—

. . . . .

"(2) that a receiver or trustee has been appointed for or has taken charge of all or the greater portion of the property of the corporation in a pending equity proceeding; or

. . . . .

"(4) that a proceeding to foreclose a mortgage or to enforce a lien against all or the greater portion of the property of the corporation is pending; or"

"Sec. 137. Prior to the first date set for the hearing provided in section 161 of this Act, an answer controverting the allegations of a petition by or against a debtor may be filed by any creditor or indenture trustee or, if the debtor is not insolvent, by any stockholder of the debtor.

"Sec. 144. If an answer filed by any creditor, indenture trustee, or stockholder shall controvert any of the material allegations of the petition, the judge shall, as soon as may be, determine, without the intervention of a jury, the issues presented by the pleadings and enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith and that the material allegations are sustained by the proofs, or dismissing it if not so satisfied.



*Appendix*

"Sec. 146. Without limiting the generality of the meaning of the term "good faith", a petition shall be deemed not to be filed in good faith if—

\* \* \* \* \*

"(3) it is unreasonable to expect that a plan of reorganization can be effected; or

"(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.

"Sec. 161. The judge shall fix a time of hearing, to be held not less than thirty days and not more than sixty days after the approval of the petition, of which hearing at least thirty days' notice shall be given by mail to the creditors, stockholders, indenture trustees, the Securities and Exchange Commission and such other persons as the judge may designate, and, if directed by the judge, by publication in such newspaper or newspapers of general circulation as the judge may designate.

"Sec. 162. At the hearing required by section 161 of this Act, or at any adjournment thereof, or, upon application, at any other time, the judge may hear objections to the continuance of the debtor in possession, or to the retention in office of a trustee upon the ground that he is not qualified or not disinterested as provided in section 158 of this Act.

"Sec. 216. A plan of reorganization under this chapter—

\* \* \* \* \*

"(10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; \* \* \* the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein; \* \* \*



*Appendix*

"Sec. 256. A petition may be filed under this chapter notwithstanding the pendency of a prior mortgage foreclosure, equity, or other proceeding in a court of the United States or of any State in which a receiver or trustee of all or any part of the property of a debtor has been appointed or for whose appointment an application has been made."

**Sections of General Corporation Act of New Jersey (Title 14, Chapter 14, Revised Statute of New Jersey, 1937; N. J. S. A. 14: 14).**

Chapter 14. INSOLVENCY, RECEIVERS AND  
REORGANIZATION.

Article 1. INSOLVENCY AND RECEIVERS.

14:14-3. INJUNCTION AND RECEIVER; APPLICATION TO COURT OF CHANCERY. When any corporation shall become insolvent or shall suspend its ordinary business for want of funds to carry on the same, or if its business has been and is being conducted at a great loss and greatly prejudicial to the interest of its creditors or stockholders, any creditor, or any stockholder who owns at least ten per cent of the capital stock of the corporation, may, by petition or bill of complaint setting forth the facts and circumstances of the case, apply to the court of chancery for an injunction and the appointment of a receiver or receivers or trustees.

The court being satisfied by affidavit or otherwise of the sufficiency of the application, and of the truth of the allegations contained in the petition or bill, and upon such notice as the court by order may direct, may proceed summarily to hear the affidavits, proofs and allegations of the parties.



*Appendix*

If upon such inquiry it shall appear to the court that the corporation has become insolvent and is not about to resume its business in a short time thereafter, or that its business has been and is being conducted at a great loss and greatly prejudicial to the interest of its creditors or stockholders, so that its business cannot be conducted with safety to the public and advantage to the stockholders, it may enjoin the corporation and its officers and agents from exercising any of its privileges or franchises and from collecting or receiving any debts, or paying out, selling, assigning or transferring any of its real or personal property whatsoever, except to a receiver appointed by the court, until the court shall otherwise order.

\* \* \* \* \*

14:14-7. POWERS OF RECEIVER; PAYMENT OF DEBT WITHOUT NOTICE OF INSOLVENCY. The receiver shall have full power and authority to demand, sue for, collect, receive and take into his possession all the real and personal property of every description, rights, credits, books and papers of the corporation, and to institute suits at law or in equity for the recovery of any property, damages or demands existing in favor of the corporation, and to sell, convey and assign all such estate, rights and interest, and shall hold and dispose of the proceeds thereof under the directions of the court of chancery.

\* \* \* \* \*

14:14-9. PROPERTY, FRANCHISES, ETC., TO VEST IN RECEIVERS OR TRUSTEES; INSOLVENT FOREIGN CORPORATIONS.  
a. All the real and personal property of a corporation for which a receiver shall be appointed under the provisions of this chapter, wheresoever situated, and all its franchises, rights, privileges, credits and effects shall, upon the appointment of a receiver or trustee, or receiver



*Appendix*

ers or trustees, forthwith vest in him or them, and the corporation shall be divested of the title thereto. \* \* \*

14:14-10. RECONVEYANCE OF PROPERTY ON PAYMENT OF DEBTS; DISSOLUTION. When a receiver has been appointed as aforesaid and it shall afterwards appear that the debts of the corporation have been paid or provided for, and that there remains or can be obtained by further contribution sufficient capital to enable it to resume its business, the court of chancery may, in its discretion, a proper case being shown, direct the receiver to reconvey to the corporation all its property, franchises, rights and effects, and thereafter the corporation may resume control of and enjoy the same as fully as if the receiver had never been appointed.

In every case in which the court of chancery shall not direct such reconveyance, it may, in its discretion, make a decree dissolving the corporation and declaring its charter forfeited and void.

14:14-14. LIMITATION OF TIME TO PRESENT CLAIMS. The court of chancery may limit the time within which creditors shall present and make proof to the receiver of their respective claims against the corporation, and may bar all creditors and claimants failing so to do, within the time limited, from participating in the distribution of the assets of the corporation. The court may also prescribe what notice, by publication or otherwise, shall be given to creditors of such limitation of time.

14:14-15. PRESENTATION OF CLAIMS; EXAMINATION. Every claim against an insolvent corporation shall be presented to the receiver in writing and upon oath, and the claimant, if required, shall submit himself to such



*Appendix*

examination and produce such books and papers relating thereto as the receiver shall direct. The receiver may examine, under oath or affirmation, all witnesses produced before him touching the claims, and shall pass upon and allow or disallow the same, or any part thereof, and notify the claimants of his determination.

\* \* \* \* \*

14:14-20. **SALE OF CORPORATE PROPERTY.** Where property of an insolvent corporation is at the time of the appointment of a receiver encumbered with mortgages or any other lien, the legality of which is questioned, and the property is of a character materially to deteriorate in value pending the litigation, the court of chancery may order the receiver to sell the same, clear of encumbrances, at public or private sale, for the best price that can be obtained, and pay the money into court, there to remain subject to the same liens and equities of all parties in interest as was the property before the sale, to be disposed of as the court shall direct.

14:14-23. **DISTRIBUTION OF ASSETS; PRIORITY OF CREDITORS.** After payment of all allowances, expenses and costs, and the satisfaction of all special and general liens upon the funds of the corporation to the extent of their lawful priority, the creditors shall be paid proportionately to the amount of their respective debts, excepting mortgage and judgment creditors when the judgment has not been by confession for the purpose of preferring creditors. The creditors shall be entitled to distribution on debts not due, making in such case a rebate of interest, when interest is not accruing on the same.

The surplus funds, if any, after payment of the creditors and the costs, expenses and allowances aforesaid, and the preferred stockholders, shall be divided and paid



*Appendix*

to the general stockholders proportionately, according to their respective shares.

\* \* \* \* \*

## Article 2. REORGANIZATION.

### A. IN GENERAL.

14:14-36. REORGANIZATION BY STOCKHOLDERS. When a majority in interest of the stockholders of a corporation, for which a receiver or trustee has been appointed, shall have agreed on a plan for the reorganization of the corporation and a resumption by it of the management and control of its property and business, the corporation may, with the consent of the court of chancery, upon the reconveyance to it of its property and franchises, mortgage the same for such amount as may be necessary for the purposes of the reorganization, and may issue bonds or other evidences of indebtedness, or additional stock, or both, and use the same for the full or partial payment of the creditors who will accept the same, or otherwise dispose of the same for the purposes of the reorganization.

### B. REORGANIZATION BY JUDICIAL SALE.

14:14-37. REORGANIZATION BY PURCHASERS OF CORPORATE PROPERTY. When the property and franchises of a corporation of this state, except steam railroad, canal, turnpike or plank road companies, shall be sold and conveyed under or by virtue of a decree of the court of chancery of this state, or of the district court of the United States in and for the district of New Jersey sitting in equity, and an execution issued thereon, to satisfy any mortgage debt, judgment, or other encumbrance thereon, such sale and conveyance, duly made and executed, shall



*Appendix*

vest in the purchaser thereof, all the right, title, interest, property, possession, claim and demand in law and equity of the parties to the suit or action in which the decree was made, of, in and to the property so sold and its appurtenances and also of, in and to the corporate rights, liberties, privileges and franchises of such corporation, but subject to all the conditions limitations, restrictions and penalties of such corporation concerning the same.

14:14-38. PURCHASERS CONSTITUTED BODY CORPORATE; RIGHTS, RESTRICTIONS, ETC. Such purchaser and his associates, not less than three in number shall thereupon be a new corporation, by the name they shall select, and shall be deemed the stockholders of the capital stock of such new corporation, in the ratio and according to the amount of the purchase money respectively contributed by them, and shall be entitled to all the rights, liberties, privileges and franchises and be subject to all conditions, limitations, restrictions and penalties of the corporation whose property and franchises shall have been so sold and conveyed, which were contained in the act or acts by or under which such corporation was created, and the supplements thereto, so far as the same were in force and unrepealed at the time of the sale and conveyance.

14:14-39. MEETING FOR ORGANIZATION OF NEW CORPORATION. The persons for or on whose account any such property and franchises may have been purchased, shall meet at the county seat of the county wherein the sale may have been made, within thirty days after the conveyance made by virtue of such process or decree shall have been delivered, written notice of the time and place of such meeting having been given to each of such persons at least ten days before the meeting, and shall organize the new corporation by electing a president and



*Appendix*

board of directors, to hold office until the first Monday of May succeeding the meeting, when, and annually thereafter on that day a like election shall be held for a president and directors to serve for one year.

14:14-40. CORPORATE NAME AND SEAL; CAPITAL STOCK; PREFERRED STOCK. At the meeting such persons shall adopt a corporate name and seal, determine the amount of the capital stock of the corporation, and may make and issue certificates of stock in shares of fifty dollars each.

The corporation may then, or at any time thereafter, create and issue preferred stock to such an amount and at such times as it may deem necessary.

14:14-41. CERTIFICATE OF REORGANIZATION; FILING; EVIDENCE. The new corporation shall, within one month after its organization, make a certificate thereof, under its common seal and signed by its president, setting forth:

- a. The date of its organization;
- b. The name so adopted;
- c. The amount of capital stock; and
- d. The names of its president and directors.

Such certificate shall, within said one month, be transmitted to the secretary of state, to be filed in his office and there remain of record. A certified copy of the certificate so filed shall be evidence of the corporate existence of the new corporation.

14:14-42. BORROWING MONEY; BONDS SECURED BY MORTGAGE. Any corporation created under sections 14:14-37 to 14:14-41 of this title may borrow such sums of money



*Appendix*

as may be necessary for the accomplishment of its objects, not exceeding at any one time the total amount of the authorized capital stock of the corporation or any increase thereof.

The corporation may secure the repayment of the whole or any part thereof, may issue bonds registered or with coupons or interest certificates attached thereto, or both, secured by a mortgage of any or all of its franchises, real or personal property, including stocks and securities of the corporation or of any other corporation whose stocks or securities it owns.

Such mortgage may be recorded as mortgages of real estate are or hereafter may be by law required to be recorded in the office of the clerk or register of deeds of the county in which the property is located and in which the principal office of the corporation is situated, and such record or the lodgment of such mortgage in such clerk's or register's office for record shall have the same force, operation and effect as to all judgment creditors, purchasers or mortgagees in good faith as the record or lodgment for that purpose of mortgages of real estate now have, although such mortgage may not have been executed, proved or recorded as a chattel mortgage.

14:14-43. PRIOR LIENS; IMPAIRMENT. Nothing contained in this article shall divest or in any manner impair the lien of any prior mortgage or other encumbrance upon the property or franchises conveyed under the sale of such property or franchises, when by the terms of the process or decree under which the sale has been made, or by operation of law, the sale is made subject to the lien of any such prior mortgage or other encumbrance, and no such sale and conveyance or organization of such new corporation shall in any way affect or impair any



*Appendix*

rights, in law or equity, of any person, not a party to the suit or action in which the decree was made, nor of any party, except so far as determined by the decree.

When any trustee shall be made a party to such suit or action, and the cestui que trust, for any reason satisfactory to the court in which the suit or action may be, shall not be made a party thereto, the rights and interests of the cestui que trust shall be concluded by such decree.











# INDEX

	Page
Opinions below.....	2
Jurisdiction.....	2
Question presented.....	2
Statutes involved.....	3
Statement.....	4
Argument.....	11
Conclusion.....	18

## CITATIONS

### Cases:

<i>Bahler v. Robert Treat Baths</i> , 100 N. J. Eq. 525.....	15
<i>Case v. Los Angeles Lumber Products Co.</i> , 308 U. S. 106.....	17
<i>Country Life Apartments v. Buckley</i> , 145 F. 2d 935.....	17
<i>Duparquet Huot &amp; Moneuse Co. v. Evans</i> , 297 U. S. 216..	14
<i>Fidelity Assurance Association v. Sims</i> , 318 U. S. 608.....	16
<i>Julius Rochrs Co., In re</i> , 115 F. 2d 723.....	18
<i>Lorraine Castle Apartments Bldg. Corp., In re</i> , 149 F. 2d 55, petitions for certiorari filed June 25, 1945, Nos. 164, 165, this Term.....	17
<i>Marine Harbor Properties v. Manufacturers Trust Co.</i> , 317 U. S. 78.....	12, 13, 14
<i>Morse et al. v. Shangold et al.</i> , 135 N. J. Eq. 350.....	15
<i>Patent Cereals v. Flynn</i> , 149 F. 2d 711.....	17
<i>Securities &amp; Exchange Commission v. United States Realty &amp; Improvement Co.</i> , 310 U. S. 434.....	14
<i>Sheridan View Building Corporation, In the Matter of (Collins v. Seifried)</i> , No. 250, this Term.....	11, 12

### Statutes:

Bankruptcy Act, Chapter X, as amended, 52 Stat. 883 (11 U. S. C. 501 <i>et seq.</i> ):	
Sec. 130.....	3
144.....	3
146.....	3, 8, 14, 16, 18
156.....	8, 13
158.....	8
161.....	8
162.....	8
208.....	2
216.....	18
256.....	4



## Statutes—Continued

	Page
General Corporation Act of New Jersey (Title 14, Chapter 14, Revised Statutes of New Jersey, 1937, N. J. S. A. 14:14)-----	4, 7
H. Rep. No. 1409, 75th Cong., 1st Sess., p. 37-----	14
Katz, <i>The Protection of Minority Bondholders in Foreclosures and Receiverships</i> , 3 U. of Chi. L. Rev. 517 (1936)-----	15
N. J. S. A. 14:14-20-----	15
Weiner, <i>Conflicting Functions of the Upset Price in a Corporate Reorganization</i> , 27 Col. L. Rev. 132 (1927)-----	15



# In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 264

---

IN THE MATTER OF ST. CHARLES HOTEL COMPANY,  
DEBTOR

---

EDWARD S. LADIN, PETITIONER

v.

HOWARD K. HURWITH, FRANK K. VIDLER; ABRAHAM H. KURZROCK; MAX N. CAROL, FIDELITY-PHILADELPHIA TRUST COMPANY, J. HENRY SCATTERGOOD, HALSTEAD RHODES, ALBERT A. LIEBERMAN; ST. CHARLES HOTEL COMPANY; AARON SMITH, TRUSTEE OF ST. CHARLES HOTEL COMPANY, DEBTOR; AND SECURITIES AND EXCHANGE COMMISSION, RESPONDENTS

---

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT*

---

## MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION IN SUPPORT OF THE PETITION

The Securities and Exchange Commission became a party to the District Court proceedings for the reorganization of the Debtor pursuant to



the provisions of Section 208 of the Bankruptcy Act, 11 U. S. C. 608. The Commission also participated as an appellee in the appeal before the Circuit Court of Appeals for the Third Circuit. The petition for a writ of certiorari, which it supports in this memorandum, and which was filed by a minority first mortgage bondholder of the Debtor, names the Commission as a respondent.

#### OPINIONS BELOW

The opinion of the District Court (R. 71a) is reported at 60 F. Supp. 322. The *per curiam* opinion of the Circuit Court of Appeals affirming the opinion of the District Court (R. 125) is reported in 149 F. 2d 645.

#### JURISDICTION

The decree of the Circuit Court of Appeals was entered on June 13, 1945 (R. 126). The petition for a writ of certiorari was filed on July 27, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, 28 U. S. C. 347 (a).

#### QUESTION PRESENTED

Whether a Chapter X bankruptcy petition must be dismissed in favor of a recently instituted equity receivership proceeding because it appears that a single class of creditors has a preponderant interest in the Debtor's assets, despite a clash of interests within the class and indications that the situation presented is fraught with the possibility



of inequitable conduct operating to the detriment of unorganized security holders.

#### STATUTES INVOLVED

The following sections of Chapter X of the Bankruptcy Act provide:

Section 130, 11 U. S. C. 530:

Every petition shall state \* \* \*

(5) the nature of all pending proceedings affecting the property of the corporation known to the petitioner or petitioners and the courts in which they are pending \* \* \*

(7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter XI of this Act; \* \* \*

Section 144, 11 U. S. C. 544:

If an answer filed by any creditor, indenture trustee, or stockholder shall controvert any of the material allegations of the petition, the judge shall, as soon as may be, determine, without the intervention of a jury, the issues presented by the pleadings and enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith and that the material allegations are sustained by the proofs, or dismissing it if not so satisfied.

Section 146, 11 U. S. C. 546:

Without limiting the generality of the meaning of the term "good faith" a peti-



tion shall be deemed not to be filed in good faith if \* \* \*

(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.

Section 256, 11 U. S. C. 656:

A petition may be filed under this chapter notwithstanding the pendency of a prior mortgage foreclosure, equity, or other proceeding in a court of the United States or of any State in which a receiver or trustee of all or any part of the property of a debtor has been appointed or for whose appointment an application has been made.

The pertinent provisions of the General Corporation Act of New Jersey (Title 14, Chapter 14, Revised Statutes of New Jersey, 1937, N. J. S. A. 14: 14) are set forth in the appendix to the petition for certiorari, pp. 21 to 29, and need not be repeated here.

#### STATEMENT

The Debtor owns a boardwalk hotel in Atlantic City, New Jersey. The property is subject to two issues of mortgage bonds: (1) \$2,228,000 principal amount of first mortgage bonds, and (2) \$153,900 principal amount of general mortgage bonds (secured by a second mortgage on the Debtor's fixed assets). The Debtor's capital stock consists of \$452,000 par value of 7% cumulative preferred stock and 9,144 3/10 shares of no par value common stock (R. 5a-6a, 52a-53a).



Petitioner and the respondent bondholders are all holders of the first mortgage bonds. These bonds were issued and sold to the public pursuant to an indenture, dated May 1, 1925, between the Debtor and Franklin Trust Company of Philadelphia, indenture trustee. In October 1931 the indenture trustee was taken over by the Secretary of Banking of the Commonwealth of Pennsylvania as an insolvent banking institution and no successor trustee has been appointed to act in its place. Although sinking fund defaults have existed since November 1928 and interest has not been paid since November 1932, no action to foreclose the first mortgage has ever been instituted (R. 52a-53a, 54a).

The general mortgage bonds were issued to the public in April 1928 pursuant to an indenture between the Debtor and Real Estate Land Title and Trust Company, indenture trustee. These bonds also have been in default since at least 1932 (R. 26a, 53a).

On the basis of facts appearing in the record it is clear that the Debtor is insolvent. In addition, the book value of its mortgaged assets, listed at \$1,417,819 as of October 31, 1944 (R. 11a), is insufficient to satisfy the claim of the first mortgage bonds for principal and accrued interest. There are indications that the book value may exceed the actual fair value of the mortgaged assets (R. 21a, 27a-28a, 31a). However, the Debtor also owns unmortgaged assets, consisting of cash



and securities, which exceeded \$115,000 in amount on October 31, 1944 (R. 10a, 53a-54a). The free assets are subject to the claim of the general mortgage bonds and the deficiency claim of the first mortgage bonds. The Debtor's hotel is under lease on a percentage basis and the present earnings produce an operating profit after taxes but before interest charges on the two bond issues (R. 29a, 49a).

Hence, the Debtor has long been in need of readjustment of its debt structure. The problem of initiating judicial proceedings for this purpose was considered by officers of the Debtor for a number of years and early in October, 1944, in view of the elimination of tax arrears, the management determined to file a voluntary petition under Chapter X of the Bankruptcy Act. The proposed petition and a form of directors' resolution were prepared by counsel. At a meeting on October 31, 1944, the directors adopted a resolution authorizing the filing of the Chapter X petition and the president verified the petition on November 9, 1944. Apparently because of a delay in the preparation of an accountant's statement, however, the petition was not filed until December 8, 1944. On the same day the petition was approved and a trustee appointed (R. 8a, 9a, 47a-48a, 49a-51a).

Nine days prior to the filing and approval of the Chapter X petition, on November 29, 1944,



respondents Hurwith and Vidler and two other bondholders filed a bill in equity in the court of the Chancellor of the State of New Jersey praying for the appointment of a receiver and ancillary relief under Chapter 14:14 of New Jersey Revised Statutes (R. 19a-20a, 22a-33a). No temporary or permanent receiver had been appointed in the state court action when the Chapter X petition was filed, and the District Court was advised of the status of the pending action before approving the Chapter X petition (R. 42a, 48a, 51a). The complainants in the chancery court included bondholders who had recently acquired their holdings and who, according to the statement of their counsel, may be interested in purchasing the mortgaged property in the event of its sale (R. 52a, 68a).

Subsequent to the entry of the order of approval of the Chapter X proceeding, which contained a stay of all other proceedings against the Debtor, counsel for Hurwith and Vidler informally advised the District Judge that in all probability a motion would be made to dismiss the Chapter X petition. Somewhat later, however, following conferences with counsel for the Debtor, their attorneys informed the District Judge that if they were appointed co-trustee and co-counsel to the trustee in the Chapter X proceeding, they would have no further interest in moving for dismissal. The attorneys stated in



substance that such appointments would assure their clients a measure of control over the Chapter X proceeding and would assure adequate fee allowances to the attorneys, thus placing both in a position substantially equivalent to that which they had reason to expect would exist in the state court action. This proposal was made in the presence of representatives of the Securities and Exchange Commission who pointed out that in their view the respondents' attorneys, as representatives of bondholders, were not eligible for the suggested appointments because of the statutory requirements relating to disinterestedness (R. 64a-69a, 108a-109a).<sup>1</sup>

A few days thereafter Hurwith and Vidler filed answers attacking the Debtor's petition as lacking in "good faith" within the meaning of Section 146 (3), (4), 11 U. S. C. 546 (3), (4), and obtained an order to show cause why the Chapter X proceeding should not be dismissed (R. 14a-33a, 34a-37a). Notice of the application for dismissal was given to the Debtor, the Chapter X trustee, and the Securities and Exchange Commission (R. 34a-35a); no notice of the order to show cause or of the filing of the answers was given to the bondholders generally (R. 96a-99a, 103a-104a).<sup>2</sup>

---

<sup>1</sup> See Secs. 156, 158, 11 U. S. C. 556, 558.

<sup>2</sup> Creditors and stockholders were given the customary notice that the Chapter X petition had been filed and that a hearing would be held pursuant to Sections 161 and 162 (11 U. S. C. 561, 562) to consider objections to the trustee's retention in office (R. 13a).



On the return day the District Judge was requested to fix a date for a trial of the issues presented by the pleadings. He indicated, however, that he preferred to hear the matter on affidavits and no opportunity was afforded to adduce evidence by oral testimony (R. 39a-40a, 41a-42a, 44a-45a, 46a, 72a).<sup>3</sup> Throughout the proceedings which followed, the Debtor displayed a purely passive attitude toward the challenge to its Chapter X petition and took no active part in the controversy (R. 62a-63a, 69a, 104a). In this connection the record shows that the Debtor's management and equity interests hold approximately 50% in amount of the first mortgage bonds (R. 53a).<sup>4</sup> At the same conference in chambers at which the attorneys for Hurwith and Vidler, with the acquiescence of counsel for the Debtor, made their unsuccessful proposal for court appointments, Commission counsel stated, in emphasis of the need for a completely disinterested trustee,<sup>5</sup>

---

<sup>3</sup> The opinion of the District Court states that the record upon which its determination was made included statements contained in argument of counsel (R. 78a, 79a, 80a).

<sup>4</sup> The bonds are held by Harry L. Katz, president of the Debtor; Emanuel Katz, his brother and a principal in the lessee company; and members of their families (R. 53a).

<sup>5</sup> As a result of a study of the qualifications of the trustee appointed by the District Judge, the Commission reached the conclusion that he did not meet the standards of disinterestedness envisioned by the statute because of relationships with the Debtor's management. When this



that preliminary investigation revealed the need for a searching inquiry into the facts and circumstances surrounding the acquisition of the bonds held by the management and equity owners for the purpose of determining whether grounds existed for equitable limitations or subordination of these bonds as against public holders (R. 66a-67a, 106a-107a). Thereafter, as stated by the District Judge, the Debtor's interest in the Chapter X proceeding lagged (R. 72a, 74a, 78a).

Following the submission of affidavits and the hearing of arguments, the District Judge filed an opinion, which noted among other things the lack of any equity in the Debtor's hotel property beyond the interest of the first mortgage bondholders and held that it was unnecessary to consider the adequacy of the state proceeding, judged by reorganization standards for the protection of creditors, since the court believed foreclosure or its equivalent would be the inevitable result. Accordingly, dismissal of the Chapter X petition was directed. (R. 71a-90a.) Notice of this determination was given to all creditors and stockholders in connection with notice of a hearing to consider the trustee's account and allowance applications. Thereafter the petitioner, who had had

view was conveyed to the District Judge and the trustee, the latter agreed to resign at the hearing required by Section 161, but in view of the pendency of the dismissal application, this hearing was adjourned from time to time (R. 47a, 70a, 72a). The decision to dismiss the Chapter X proceeding rendered disposition of the matter unnecessary.



no previous notice of the application to dismiss, moved to vacate the dismissal and for a trial of the issues presented by the pleadings (R. 93a-101a). At the hearing on this application, other first mortgage bondholders appeared in support of the petitioner (R. 107a-108a). The District Judge denied the motion (R. 109a-110a). Petitioner thereupon appealed to the Circuit Court of Appeals for the Third Circuit. On June 13, 1945, the circuit court, in a *per curiam* opinion (R. 125), affirmed the orders of the District Court on the latter's opinion. The instant petition for a writ of certiorari followed.

#### ARGUMENT

##### I

The importance of the question presented by the petition in this case and in *In the Matter of Sheridan View Building Corporation (Collins v. Seifried)*, No. 250, this Term, is discussed in a memorandum which the Securities and Exchange Commission is filing as *amicus curiae* in support of the latter petition, at pp. 8-19, to which the Court is respectfully referred. The coincidence of these two cases emphasizes the recurrent nature of the problem involved and the need of a decision by this Court if creditors who may have ulterior motives are to be prevented from forestalling Chapter X proceedings by the precipitate commencement of receivership or foreclosure suits from which they may derive unfair advantage.



## II

A. The instant case, like that of the *Sheridan View Building Corporation*, involves a clash of interests among a single class of bondholders of the very type which should have compelled the court below and the District Court to weigh the relative advantages and particular benefits of Chapter X as against "the older procedures which Chapter X was designed to improve and supplant" (*Marine Harbor Properties v. Manufacturers Trust Co.*, 317 U. S. 78, 87).

Included in the group which instituted the state court proceeding and moved for the dismissal of the Chapter X petition are bondholders with recently acquired holdings who have expressed their interest in purchasing the property in the event of its sale. In argument and in briefs submitted to the District Judge, counsel for this group stated that it was their purpose to direct the state court proceeding toward a sale. While the matter would have been explored further had there been an opportunity to produce oral testimony, it is a permissible inference from so much as has already been disclosed that the bondholders who seek to sustain the state court proceeding may wish to serve their own self interest in that proceeding, which they hope to dominate (see R. 67a-68a), thus endangering the interests of other bondholders.



By comparison, in *Marine Harbor Properties v. Manufacturers Trust Co.*, *supra*, the independent and disinterested mortgage trustee, by virtue of its rights as an absolute owner of the mortgage under the broad declaration of trust, was in a position to protect all the senior bondholders by taking the property at the foreclosure sale in the prior proceedings for their exclusive benefit. No comparable protection is available at a sale in the New Jersey equity proceeding or in an ordinary foreclosure sale under New Jersey law. On the other hand, the important safeguards contained in Chapter X would insure a fair and equitable plan, protecting minority bondholders from a sale at an inadequate price and from the danger of being squeezed out of the enterprise with inadequate compensation. Through its independent and disinterested trustee (Section 156, 11 U. S. C. 556), the Chapter X court could obtain informed and independent advice concerning the type of plan adapted to serve the best interests of creditors<sup>6</sup> and others affected, including the

---

<sup>6</sup> In this connection, consideration must be given to the interests of the second mortgage bondholders and unsecured creditors. As distinguished from the *Marine Harbor* case, this case involves a Debtor who owns substantial unmortgaged assets, aggregating in excess of \$115,000, in which these junior creditors have a *prima facie* interest on a parity with the deficiency claim of the first mortgage bondholders. (R. 10a, 53a-54a.) The relative claims upon the free assets will depend upon the amount of the deficiency claim of the senior creditors and this, in large measure, will be determined by the results of the sale or other readjustment effected. Hence



possibility of a sale to a suitable purchaser dependent upon an arm's length bid of an adequate price.

The pending equity receivership in the state court is subject to the traditional limitations which Congress intended to supplant and improve in enacting bankruptcy reorganization legislation. H. Rep. No. 1409, 75th Cong., 1st Sess., p. 37 *et seq.*; *Duparquet Huot & Moneuse Co. v. Evans*, 297 U. S. 216; *Securities & Exchange Commission v. United States Realty & Improvement Co.*, 310 U. S. 434, 448-450. Thus there is no machinery to bind dissenters to a plan;<sup>7</sup> no requirement for

---

the instant situation actually presents a "reorganization proceeding dealing with more than one class of securities under the older procedures which Chapter X was designed to improve and supplant" (317 U. S., at 87). In such circumstances, "the safeguards afforded by Chapter X would have specific significance in protecting the respective classes of investors against improvident, unfair or inequitable adjustments, compromises, and settlements—steps which are basic to the reorganization process but which in selfish hands led to much abuse" (*ibid.*). Under such circumstances, in the words of this Court, the relative advantages and particular benefits of the Chapter X machinery become "highly relevant and persuasive" (*ibid.*).

<sup>7</sup> It is assumed *arguendo* that the "prior pending" proceeding for purposes of Section 146 (4) may be deemed to include not only the actually pending suit for a receivership but also the possibility of a foreclosure sale, this would require the appointment of a successor indenture trustee, the institution by the successor trustee of a foreclosure suit, and the consolidation of that suit with the receivership proceeding. Without these further steps the existing receivership proceeding could not lead to a sale, or to a plan, since the statutory procedure for sale by a receiver applies to mort-



judicial scrutiny of the plan under standards comparable to the "fair and equitable" and "feasible" standards of Chapter X; and no machinery assuring disinterested leadership in the formulation of a plan. There is only the somewhat indirect scrutiny of a plan on the point of fruition, incident to confirmation of a foreclosure sale by the equity court in which the traditional tendency has been to confirm sales at any price not so inadequate as to shock the conscience of the court. See Katz, *The Protection of Minority Bondholders in Foreclosures and Receiverships*, 3 U. of Chi. L. Rev. 517 (1936); Weiner, *Conflicting Functions of the Upset Price in a Corporate Reorganization*, 27 Col. L. Rev. 132 (1927); *Morse et al. v. Shengold et al.*, 135 N. J. Eq. 350 (1944).

The state court proceeding has no requirement for an independent trustee. Here the Chapter X safeguard seems particularly pertinent in view of (1) the suggestion of causes of action against the management interests and of equities requiring subordination or limitation of their claims (R. 66a-67a, 106a-107a), (2) the concern of the creditor who instituted the state court proceedings to influence the selection of the receiver and his counsel (R. 64a-69a, 108a-109a), (3) the

---

gaged property only when the title is in dispute and the property itself is in danger of deterioration, as to which there is no present suggestion. See N. J. S. A. 14: 14-20 (Appendix to petition, p. 24); *Bahler v. Robert Treat Baths*, 100 N. J. Eq. 525 (1927).



debtor's loss of interest in the Chapter X proceeding and absence of opposition to the receivership, which in effect converts the state court proceeding into a consent receivership, and (4) the ownership by the management and equity interests of approximately 50% of the bonds. The pertinent inadequacies of the state court proceeding as compared to Chapter X were not considered by the District Judge, who deemed his action to be controlled by the *Marine Harbor* case and stated "we need not examine the difference between the two procedures" (R. 83a). There was thus no actual determination of whether the interests of the Debtor's bondholders would actually be "best subserved" in the prior proceedings in accordance with the test prescribed in Section 146 (4).

B. The District Judge also intimated that the Chapter X petition was not filed in good faith within the meaning of Section 146 (3), 11 U. S. C. 546 (3), because of an alleged lack of proof as to the possibility of reorganization, citing *Fidelity Assurance Association v. Sims*, 318 U. S. 608. We do not discuss this aspect of the case in detail since the District Court's holding apparently turned primarily upon the issue of good faith as related to the prior proceeding. The *Sims* case, however, stands merely for the proposition that a petition under Chapter X must be dismissed for failure to meet the statutory requirement of "good faith" if it appears at its inception that



the only possible accomplishment of the Chapter X proceedings would be piecemeal liquidation of the debtor's assets as in an ordinary bankruptcy. *Country Life Apartments v. Buckley*, 145 F. 2d 935 (C. C. A. 2); *In re Lorraine Castle Apartments Bldg. Corp.*, 149 F. 2d 55 (C. C. A. 7), petitions for certiorari filed June 25, 1945, Nos. 164, 165, this Term; *Patent Cereals v. Flynn*, 149 F. 2d 711 (C. C. A. 2).

Such is not the present case. The Debtor's mortgaged property is being operated under a lease as a going concern and its operations are producing a profit prior to interest charges (R. 49a). There is no doubt that the Debtor can be reorganized as a going concern with creditor participation, and the fact that stockholders are likely to be excluded because of failure to offer any new contributions of capital does not, contrary to the conclusion of the District Court (R. 88a), rule out the possibility of a "reorganization". On the contrary, plans completely excluding stockholders are often the result of proceedings commenced by petition of an insolvent debtor. See *Case v. Los Angeles Lumber Products Co.*, 308 U. S. 106, at 131. Among other customary reorganization possibilities, a plan might provide for (1) a transfer of the mortgaged property to a reorganized company in which bondholders alone might participate or (2) a sale of the entire property at a fair price and



distribution of the proceeds among the bondholders. There is no necessity of showing at the inception of a Chapter X proceeding that a particular plan or plans can actually be formulated. See *In re Julius Roehrs Co.*, 115 F. 2d 723, 724 (C. C. A. 3). This is not a case, such as that envisaged by Section 146 (3), in which reorganization can afford no workable solution and where, as in the *Sims* case, the piecemeal liquidation of a bankruptcy proceeding is the only feasible course. The possibility that an acceptable bidder may be found, rendering it desirable to adopt a plan involving a sale at a fair upset price, is certainly not a bar to the approval of the Chapter X petition, since this possibility is expressly recognized by Section 216 (10) of the Act and the procedure is there sanctioned as permissible under Chapter X.

#### CONCLUSION

By virtue of the foregoing, it is respectfully submitted that the instant petition for a writ of certiorari should be granted.

HAROLD JUDSON,  
*Acting Solicitor General.*

ROGER S. FOSTER,  
*Solicitor, Securities and Exchange Commission.*

AUGUST 1945.



SEP 10 1945

CHARLES ELMORE GROPLEY  
CLERK

IN THE

**Supreme Court of the United States**

OCTOBER TERM, 1945

No. 264

IN THE MATTER

*of*

ST. CHARLES HOTEL COMPANY,

Debtor.

EDWARD S. LADIN,

Petitioner.

HOWARD K. HURWITH, FRANK K. VIDLER; ABRAHAM H. KURZ-  
ROCK; MAX N. CAROL, FIDELITY-PHILADELPHIA TRUST COM-  
PANY, J. HENRY SCATTERGOOD, HALSTEAD RHODES, ALBERT  
A. LIEBERMAN; ST. CHARLES HOTEL COMPANY; AARON  
SMITH, TRUSTEES OF ST. CHARLES HOTEL COMPANY,  
Debtor; and SECURITIES AND EXCHANGE COMMISSION,

Respondents.

**MEMORANDUM SUBMITTED ON BEHALF OF RE-  
SPONDENTS HOWARD K. HURWITH AND FRANK  
K. VIDLER IN OPPOSITION TO PETITION  
FOR CERTIORARI**

ROBERT K. BELL,  
Ocean City National Bank Building,  
Ocean City, N. J.,  
Counsel for Respondents.







# INDEX

	PAGE
Statement .....	1
Argument .....	4
Conclusion .....	16

## Citations

### Cases:

In re Biltmore Grande Apartments Building Trust, 146 Fed. (2d) 81 .....	9, 11
Case v. Los Angeles Lumber Products Co., 308 U. S. 106 .....	5, 6
Country Life Apartment v. Buckley, 145 Fed. Sup. 935 .....	6
Federal Terra Cotta Co. v. Atlantic Terra Cotta Co., 133 N. J. Equ. 360, 365 .....	12
Fidelity Assurance Association v. Sims, 318 U. S. 608 .....	5, 6, 7, 8, 11, 14
In re Julius Roehrs, 115 F. 2d 723-724 (C. C. A. 3d Cir.) .....	5, 6
In re Lorraine Castle Apartments Bldg. Corporation, 53 Fed. Supp. 994, E. D. Ill. (Feb. 1944) .....	9
Marine Harbor Properties v. Manufacturers Trust Company, 317 U. S. 78 .....	9, 10, 11, 14, 16
Michel v. Necker (1918), 90 N. J. Eq., 171, 174, 175, 176 .....	12
In the Matter of Sheridan View Building Corpora- tion, 149 Fed. 2d 532, 7th Cir. ....	10
Wabash Railroad v. Adelbert College, 208 U. S. 38, 54 .....	13
Westinghouse & Electric Mfg. Co. v. Richmond Light & Railroad Co., 267 Fed. 493, 495 .....	13

### Statutes:

Bankruptcy Act, Chapter X as Amended, 52 Stat. 883 (11 U. S. C. 501 et seq.):	
Sec. 146, subd. 3 .....	4
Sec. 146, subd. 4 .....	8, 10
General Corporation Act of New Jersey (Title 14, Chap. 14 Rev. Stat. of New Jersey of 1937, N. J. S. A. 14:14) .....	12
14:14-4 .....	12, 13
14:14-11, 12, 30, 31 and 32 .....	14







IN THE  
**Supreme Court of the United States**

OCTOBER TERM, 1945

---

No. 264

---

---

IN THE MATTER  
*of*  
ST. CHARLES HOTEL COMPANY,  
  
Debtor.

---

EDWARD S. LADIN,  
  
Petitioner.

HOWARD K. HURWITH, FRANK K. VIDLER; ABRAHAM H. KURZ-  
ROCK; MAX N. CAROL, FIDELITY-PHILADELPHIA TRUST COM-  
PANY, J. HENRY SCATTERGOOD, HALSTEAD RHODES, ALBERT  
A. LIEBERMAN; ST. CHARLES HOTEL COMPANY; AARON  
SMITH, TRUSTEES OF ST. CHARLES HOTEL COMPANY,  
Debtor; and SECURITIES AND EXCHANGE COMMISSION,  
Respondents.

---

**MEMORANDUM SUBMITTED ON BEHALF OF RE-  
SPONDENTS HOWARD K. HURWITH AND FRANK  
K. VIDLER IN OPPOSITION TO PETITION  
FOR CERTIORARI**

---

**Statement**

We supplement to some extent the facts presented in the brief of the petitioner Ladin and the supporting brief of the Securities and Exchange Commission.



(a) There are really only two respondents who take a position adverse to Edward S. Ladin, the petitioner herein, i. e., Howard K. Hurwith and Frank K. Vidler. The other nine so-called respondents are necessary or interested parties who support Ladin's position.

Hurwith and Vidler were two of four First Mortgage Bondholders, who took the first step anyone had undertaken in twelve years to examine into the affairs of the Debtor, and to deprive members of the Katz family of the control they were exercising over the St. Charles Hotel for their exclusive benefit. On November 29, 1944 they instituted an action against the Debtor in the Chancery Court of the State of New Jersey for the relief afforded creditors against an insolvent corporation under 14 New Jersey Statutes (Corporation, General), Chapter 14, Sections 1 to 48 inclusive. The complaint charged, among other things, that Harry L. Katz, President of the Debtor, and the members of his immediate family, had organized Kaber Corporation in 1940, and had caused the Debtor to lease its hotel to Kaber for twenty years in order to defraud creditors generally, and First Mortgage Bondholders in particular.

Simultaneously with the filing of their complaint, the plaintiffs moved the Chancery Court for the appointment of a receiver of the Debtor's assets, pursuant to the aforesaid statute.

(b) The petition for reorganization under Chapter X was filed in the United States District Court of New Jersey nine days after the bill was filed in the Chancery Court, i. e., on December 8th, 1944. On that date, the Debtor obtained an order staying the plaintiffs in the Chancery Court from proceeding with the motion for the appointment of a receiver, or otherwise prosecuting the State Court action.

(c) The financial balance sheet which the Debtor annexed to its petition (R. 10a-12a) indicated that at the time of filing of the petition the Debtor was hopelessly insolvent.



Its liability exceeded its assets by \$3,349,043.54. This state of hopeless insolvency was not disputed by anyone in the proceedings below.

It is, therefore, not surprising to find, as is pointed out in Judge Forman's opinion, no fresh contribution of capital was offered by stockholders, or anyone else, as an aid to reorganization.

(d) Notice of hearing, under Section 161 of the Bankruptcy Act was given to all bondholders (R. 13a-14a). Only the respondents, Hurwith and Vidler, two of the four plaintiffs in the chancery suit, appeared on the ~~return~~ day, filed their answers to the petition, and moved to dismiss it for lack of jurisdiction. The Securities and Exchange Commission appeared, and opposed the dismissal, both on its behalf and on behalf of the Debtor (R. 39a). The position of Hurwith and Vidler was sustained in the District Court, and the proceedings were dismissed by order dated March 26th, 1945 (R. 98). The opinion of Forman, D. J., is to be found at R. 71a et seq.

Then the petitioner Ladin appeared for the first time. The day following the entry of the order of dismissal, he moved to vacate that order, and for a rehearing of the issues raised by the answering creditors, Hurwith and Vidler. Ladin identified himself as the owner of a single First Mortgage bond in the sum of Five hundred (\$500) Dollars, and as a securities' dealer (R. 95a-96a). The Securities and Exchange Commission supported Ladin in that application, as did several other bondholders, now named respondents, who likewise appeared on the scene for the first time. The District Judge denied the motion, by order dated April 30th, 1945 (R. 109a-110a). Ladin then appealed to the Circuit Court of Appeals for the Third Circuit, which affirmed on the opinion of Judge Forman.



## ARGUMENT

---

### I

It was conclusively demonstrated at the very threshold of the proceeding that no reorganization could be effected. Hence the District Court was required to dismiss the debtor's petition as not having been filed in "good faith" as defined by Section 146 (3) of the Bankruptcy Act.

The first mortgage indebtedness, principal and interest, totals in round figures about \$4,450,000. An *exaggerated* value of the hotel property is \$1,000,000 in round figures. *No one will contend that its utmost value exceeds that figure by any appreciable amount.* Thus, the secured indebtedness is more than four times the value of the Debtor's property. The First Mortgage Bondholders, who have not even received any interest since November 1, 1932, are now clearly entitled to apply the hotel to the satisfaction of their secured debt, though, of course, they cannot hope to satisfy that debt in full, or even in greater part. In these circumstances no reorganization is possible if no fresh money is to fall—and no one has offered any money.

Every petition filed under Chapter X of the Bankruptcy Act must be filed in "good faith" (Sec. 146). It is not deemed filed in good faith if it appears that it is unreasonable to expect that a plan of reorganization can be effected (Sec. 146, subd. 3).

There can be no reorganization if it is manifest that the contemplated changes in the affairs of the Debtor will not benefit the Debtor, or its stockholders, as well as creditors. Chapter X does not apply where the only result to be anticipated from the proceeding is a total separation of the Debtor from its assets. Chapter X is entitled "Corporate Reorganizations." "Reorganization" connotes survival. If



the Debtor has all its property taken from it, and then sinks into oblivion, it is not being "reorganized".

But the petitioners (and particularly the Securities and Exchange Commission) suggest that a reorganization within the meaning of Chapter X can be effected even though the Debtor, the owner of the business, is wholly excluded from any further interest therein. The thought behind this suggestion is that the creditors may take over the business and become its owners, and that this constitutes a reorganization.

The very contention which the Commission so makes was advanced by it in *Fidelity Assurance Association v. Sims*, 318 U. S. 608, where a motion to dismiss had been made, as in this case, under Sec. 146, subd. (3). In that case, the Commission had prevailed upon the District Court to accept that very contention (42 Fed. Sup. 973). In doing so, the District Court relied on *Case v. Los Angeles Lumber Products Co.*, 308 U. S. 106. The Circuit Court of Appeals, however, reversed the District Court (129 Fed. 2d 442), and the Supreme Court affirmed the Circuit Court. Uninstructed by these reversals, the Commission is again pressing that erroneous contention.<sup>1</sup>

---

<sup>1</sup> The Securities and Exchange Commission again urges the Case case and *In re Julius Roehrs*, 115 F. 2d 723-724 (C. C. A., 3d Cir.) for the proposition that "plans completely excluding stockholders are often the result of proceedings commenced by petition of an insolvent debtor", p. 17, supporting memorandum. This is but a half statement, or half truth. Neither case stands for such a principle. The Case case arose under former Section 77B of the Bankruptcy Act which contained no provision for attacking jurisdiction on the grounds of lack of "good faith", as can now be done under Section 146 of the present Act. After long drawn out proceedings, a plan had been promulgated in that case which gave old stockholders 23 per centum of the value of the reorganized enterprise, although they had offered to make no contribution of fresh capital. On appeal to this Court that apportionment of stock to the old stockholders was

---

(Footnote continued on next page.)



stricken from the plan of reorganization. The reason for this was that their former equity had been completely destroyed so that without capital contribution from them, they could not acquire a part of the new company. It is true that this ruling resulted in a reorganization under Section 77B, in which stockholders received no benefits. But that result followed from the special circumstances of that case under the prior statute. At no stage of the litigation had anyone raised the contention that the proceedings should be dismissed because the "reorganization" would exclude stockholders; no statutory provision then existed for dismissal on that ground; and if it had, this Court might still have retained jurisdiction on the practical ground that the litigation and the attempts at reorganization having progressed as far as they did, it would have been wasteful to dismiss at so late a stage. This pragmatic distinction was recently voiced by the Second Circuit in deciding *Country Life Apartment against Buckley*, 145 Fed. Sup. 935. Pointing out that *Fidelity Assurance Association v. Sims* stood for the proposition that a petition is not filed in good faith where liquidation and not a readjustment of the rights of creditors was at the very outset the only outcome to be expected, the Court went on to rule that since the objection was only urged at a late stage of the proceeding, it would not be entertained.

Nor does *In re Julius Roehrs Company*, *supra*, sustain the proposition advanced by the Securities and Exchange Commission. The only specific question before the Court in that case was who, in a Chapter X proceeding, had the right to submit a plan of reorganization. It ruled the Trustee alone could do so. Wholly by way of dictum, the Court wrote that the test of the sufficiency of a plan was not whether the stockholders would profit, as it might be that the plan ultimately adopted might exclude stockholders from any participation. For this statement, the Court cited the *Case* case. The Court wrote of a plan "ultimately adopted", as was the fact in the *Case* case. And it may be that in using this language it had in mind the pragmatic distinction above referred to. Be that as it may, the Third Circuit was not considering in the *Roehrs* case any attack on jurisdiction made at the outset of the proceeding. In affirming the case now at Bar, the Third Circuit seems to have recognized that the *Fidelity* case, decided by this Court two and a half years after it decided the *Roehrs* case, controlled; and that where it appeared initially that the holders of the equity would be kept from participating in the reorganized company, no "reorganization", in the statutory sense, was possible.



The trouble with the contention, as the authority of the *Fidelity* case would indicate, is that the petitioners fail to distinguish between rehabilitation of a debtor—the purpose intended to be accomplished by a proceeding under Chapter X—and liquidation of a debtor. If the debtor is wholly deprived of its property,—if all its property is taken away from it and applied to the use of creditors,—it is not rehabilitated, but liquidated. It does not matter that its creditors take over the property as a going business, and run it as owners, or whether they sell it to a third party, merely appropriating the proceeds. In either event, they have taken the debtor's property from it and applied the property to the satisfaction of the debt as effectually and with the same results, as if they had issued an execution under a judgment. There is nothing startling or novel about a creditor acquiring his debtor's property at an execution or a foreclosure sale. This is very usual procedure,—but it is no reorganization. Chapter X was obviously designed to aid corporate debtors, as well as their creditors, by enabling the debtors to rehabilitate themselves. If the contention of the Commission were sound, then there would never be a case in which the institution of a proceeding under Chapter X would not be appropriate, because there is never a case in which it is not possible, and even likely, that the creditors will take over the property. There could then never arise a case under Section 146 (3) of absence of good faith through lack of expectancy in the consummation of a plan of reorganization. If taking over a debtor's property is reorganization, that can always be “expected”.

This Court said as much in *Fidelity Assurance Association v. Sims*, 318 U. S. 608. It there rejected the argument that liquidation of a debtor was tantamount to a reorganization; and went on to say that where a suggested plan does not deal with the readjustment of the rights and interests of creditors and stockholders, there is no reorganization; “good faith” in the statutory sense is then lacking (p. 618); and the Court concluded (p. 621) with the statement that the Statute does not contemplate a liquidation in a



Chapter X proceeding, but only by ordinary bankruptcy, or a dismissal outright.

In the case at bar, as in the *Fidelity* case, "liquidation is all that could be hoped for". No one offered to supply moneys to keep the St. Charles Hotel Company "in the picture". Its stockholders must be wiped out. *It* (the present corporation) cannot continue to function as a going concern. The petitioner Ladin writes: "It is undisputed that the Debtor makes a profit before interest on its funded debts and that it is possible, by a revision of its capital structure, to enable *it* to continue to function as a going concern" (p. 17, Brief). The fallacy of this, that which begs the entire question, is the failure to recognize that the "it" which "might continue to function as a going concern" would not be this Debtor but an entity from which the present stockholders would be wholly absent.

Under the circumstances, it was not necessary to hold plenary hearings, as the Commission insisted Judge Forman do. Hearings would not have altered the basic facts that the stockholders no longer had an equity so that there could be no readjustment of the rights of creditors and stockholders, inter se. Where it thus appeared at the very outset of the proceedings that no plan of reorganization could be effected, the petition was properly dismissed, and no further review is necessary on that score.

## II

The Chapter X petition had to be dismissed since it was not filed in "good faith" as defined by Section 146, Subdivision 4 of the Bankruptcy Act. Neither petitioner Ladin, nor the Debtor, nor any other party, satisfied the burden of proof resting upon them to demonstrate that the prior state court proceedings would not best subserve the interests of creditors and stockholders.

A petition is not filed in "good faith" as defined by Section 146, subd. (4) if



“a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in any such prior proceeding.”

The petition herein, as filed, failed to meet the requirements of this provision, particularly as it was interpreted in *Marine Harbor Properties v. Manufacturers Trust Company*, 317 U. S. 78. That decision advanced two main reasons for the dismissal of the Chapter X petition. Both apply forcibly to the facts of the instant case.

The statutory provision proclaims there is no “good faith” if it be made to appear that the prior State Court proceeding best subserves the “interest of creditors and stockholders”. It does not read: “creditors or stockholders”, though petitioners herein would read it that way. When, therefore, stockholders, as in the *Marine Harbor* case, and as in this case, can have no interest in the reorganization because of their failure to make contribution of fresh moneys, the prior state court proceeding cannot possibly serve them. “Hence, such a showing does not establish on behalf of the stockholders that ‘need for relief’ which § 130 (7) read in light of Sec. 146 (4) requires”. *Marine Harbor* case (p. 86).

Under such circumstances, there is no basis and no need for determining by comparison, using “reorganization standards”, whether the stockholders can be better subserved in the state or in the federal court. Having no interest, a state court can subserve their needs just as well as a federal court under Chapter X.

The burden of proving the contrary rested upon the proponents of the debtor’s petition. The District Court properly found they failed to do so (Opinion, 89a bottom-90a) and the dismissal of the petition on that ground was correct.

The same result was reached In re *Biltmore Grande Apartments Building Trust*, 146 Fed. 2d 81, 7th Cir.; In re *Lorraine Castle Apartments Bldg. Corporation*, 53



Fed. Supp. 994, E. D. Ill. (Feb. 1944); In the Matter of *Sheridan View Building Corporation*, 149 Fed. 2d 532, 7th Cir. (Application for a Writ of Certiorari being made contemporaneously with the instant application.)

The second ground for dismissal discussed in the *Marine Harbor* case, also pertinent here, is that where only one of several classes of creditors has an interest left in the equity of a debtor, the prior proceedings will not be supplanted by a Chapter X proceeding, in the absence of a showing that the interests of that single class will be jeopardized. The burden of proving such possible injury rests upon the proponents of the Chapter X petition. (*Marine Harbor* case, pp. 86-88.)

On the question of application of that rule to this case, it were best to quote the findings and conclusions of Judge Forman.

“In fact, it appears from the record that if a plan of reorganization is effected it could consist of no more than an equivalent to a foreclosure of the rights of all creditors and stockholders other than the first mortgage bondholders. Whether the corporation be liquidated and the lienors paid off, whether foreclosure proceedings be taken and the property sold to the lienors, or whether the first mortgagees convert their bonds into stock as evidence of their ownership, the effect and net result would be the same—the first mortgage bondholders alone may participate in the proceedings and determine the ultimate form of their holdings. No showing has been made by the debtor corporation or the Securities & Exchange Commission, as the proponent of its petition, that this result cannot be obtained in the suit in the New Jersey Court. (See N. J. S. A 14:14, *supra*.)” (R. 84a-85a).

The dismissal of the petition on this additional ground under Subdivision 4, Section 146, was also correct.



## III

**Upon supposed distinctions and differences.**

Both petitioner Ladin and Securities and Exchange Commission strain to find differences between the instant case and the decisions in the *Fidelity* and *Marine Harbor* cases.

A. With reference to the point last discussed above, the Commission urges that this is not a case in which the interests of only First Mortgage Bondholders have to be administered, for there is \$115,000 in cash which also has to be properly distributed.

The existence of the \$115,000 cash makes for a distinction without a difference between this case and the *Marine Harbor* case. There is little or no distinction between the existence of a single asset, such as in the *Marine Harbor* case, and the existence here of a single large asset plus a relatively small amount of cash. That sum falls far short of meeting the claims of creditors, and the first bondholders will be entitled in any event to the greater portion of the fund.

Precedents fortify this conclusion. In the *Fidelity* case not only was there one greatly preponderant class of creditors, principally entitled to the deposits with the various State authorities and the unpledged assets of the debtor, but there was \$500,000 cash to be administered and distributed amongst all creditors. This Court found no difficulty in assuming that the West Virginia State Court would be able to administer the cash, although there were creditors in all forty-eight states of the union. In *Biltmore Grande Apartment Building Trust, supra*, First Mortgage Bondholders alone were interested in the equity. There was, however, a cash sum on hand in which other creditors were entitled to share with the bondholders. The Federal Court had no hesitancy in ruling, under the *Marine Harbor* case, that the State Court should be permitted to administer the entire estate.



B. Both petitioner Ladin, and the Commission, compare the effectiveness of a Chapter X proceeding with the New Jersey statutory proceeding. (*General Corporation Act of New Jersey*, Title 14, Chap. 14 Rev. Stat. of New Jersey of 1937, N. J. S. A. 14:14.) (Their argument in this respect assumes that comparison is pertinent, although only one class of creditors has any interest in the equity, and there can be no Chapter X reorganization because stockholders refuse to contribute fresh money.) The Commission states (p. 14, brief) that the pending prior chancery proceeding is an "equity receivership", "subject to the traditional limitations which Congress intended to supplant and improve in enacting bankruptcy reorganization legislation". Petitioner Ladin also so regards it (Vide language of brief "Question 2", p. 3). The New Jersey chancery proceeding is not an equity receivership at all. Originally, it was a *quasi quo warranto* proceeding, intended to effect dissolution. Recently it was amended to add special provisions for reorganization. The powers of the Chancery Court in the statutory proceeding are much broader than in the ordinary receivership, so much so, that the statutory action will supersede any pending equity receivership.

*Michel v. Necker* (1918), 90 N. J. Eq. 171, 174, 175, 176.

The petitioner Ladin presents another erroneous view of the New Jersey statutory action. He concludes (pp. 16-17, brief), that the statutory receiver has no power to protect the interests of the First Mortgage Bondholders herein; that a second action, for foreclosure, will have to be instituted by a substituted indenture trustee; and such action then would not be prior to the Chapter X proceeding, but subsequent to it. Section 14:14-4 of the New Jersey statute (reproduced at p. 13, below) declares that the receiver represents all creditors. There are judicial declarations to that effect in *Michel v. Necker*, *supra*, and *Federal Terra Cotta Co. v. Atlantic Terra Cotta Co.*, 133 N. J.



Equ. 360, 365. As the representative of First Mortgage Bondholders, as well as other interests, the receiver may himself obtain foreclosure relief from the Chancellor, who designated him, and who has the power to grant that relief, along with whatever else may be necessary, in the statutory proceedings. Or the receiver may cause the Chancellor to appoint a substitute indenture trustee who would bring a foreclosure action. It is elementary that a court of competent jurisdiction having once taken property into its possession through its officer, may, as an incident thereto, and as ancillary to the suit in which the possession was acquired, determine all questions respecting the title, the possession, or the control of the property. *Wabash Railroad v. Adelbert College*, 208 U. S. 38, 54. Such an ancillary proceeding might be an action of foreclosure.

*Westinghouse & Electric Mfg. Co. v. Richmond Light & Railroad Co.*, 267 Fed. 493, 495 (Chambers, J., E. D. N. Y. 1920).

Whether the receiver takes action to foreclose directly in the statutory proceeding, or causes a substituted indenture trustee to institute an ancillary foreclosure action to the main proceeding, it cannot be said that the latter would be a wholly new and independent action, subsequent to the filing of the petition under Chapter X.

C. The Commission then weighs the alleged superiority of the Chapter X proceeding over the State proceeding. First, it tips the scales by alleging that "The State Court proceeding has no requirement for an independent trustee" (brief, p. 15). The New Jersey statute (Title 14, Chapter 14, Revised Statutes of New Jersey, 1937) contains a provision, 14-4, which the petitioner Ladin did not print in his "Appendix" when he reproduced certain other provisions of that statute. 14-4 reads:

"The Court of Chancery, at the time of ordering the injunction or at any time thereafter, may appoint a receiver or receivers or trustees for the creditors and



stockholders of the corporation. The court of chancery may remove any receiver or trustee and appoint another or others in this place, or fill any vacancy which may occur."

The State Court proceeding, therefore, does make provision for an independent receiver or trustee, the Commission's statement to the contrary notwithstanding. (Such disinterested receiver has actually been appointed.)

The Securities and Exchange Commission deems the New Jersey Chancery proceedings inadequate in another respect. As certain acts of individuals connected with the Debtor should be fully investigated, the Commission urges that this could be done better under Chapter X than in the State Court.

The State statute (General Corporation Law of New Jersey) makes full and complete provision for examination of irregularities,—Section XIV—11, 12, 30, 31 and 32. The Commission again assumes gratuitously that these powers will not be exercised by the receiver appointed in the Chancery Court, or by the Court itself. The very assumption in which the Commission here indulges was specifically and sharply rejected by this Court in the *Fidelity Assurance Association* (p. 619) and in the *Marine Harbor* (p. 87) cases.

Apart from the supposed inadequacy of the New Jersey statutory machinery for investigation, the Commission is suspicious of those who are to manage that litigation—that they may fail in the task of investigating the acts of the members of the Katz family. Counsel for the Commission who handled the case in the courts below, has consistently envisaged himself as the only suitable candidate for the role of investigator. The suspicion is directed mainly at the plaintiffs in the chancery action, two of whom are respondents here. But in pretending to harbor such serious apprehensions, the Commission loses sight of the fact that



the conduct of the litigation in the New Jersey courts will not be in the hands of the plaintiffs, but in that of the independent receiver.

Even if the plaintiffs could manage the litigation, there is no ground for the apprehension that they would not do their utmost to see to it that the Katz family and their associates would disgorge any gains improperly obtained by them and that they should not benefit by purchases of first mortgage bonds at prices excessively below their face value. It is a little ironic that neither the Commission nor anyone else did anything until after the plaintiff bondholders had filed their bill in the Chancery Court of New Jersey, specifically pointing out various transgressions of the Katzes.

Motivated to some extent by the desire to control the litigation, counsel for the Commission accents the argument that the plaintiffs in the Chancery suit wish to buy the property for their own selfish interest. The very manner in which the argument is presented (p. 12, Commission's brief), reflects its inconsequential value. It is urged that "*some* of those bondholders (there are four all told) with recent acquired holdings, have expressed an interest in purchasing the property." By use of the word "*some*" the Commission escapes the necessity of stating exactly how many. The basis for this statement, however, is that counsel for the respondents said conversationally that he might ask one bondholder, who acquired his bonds almost a year before the Chancery Court suit was instituted, whether he were interested in making a bid for the property, if and when it were offered for sale. That question was never put to the bondholder, and his interest in the property was never determined. When the Commission's briefer reaches the end of that paragraph (p. 12), only a few lines down, the word "*some*" has disappeared and the unfounded, colorable inference is drawn that "*the*" bondholders, i. e., "*all*" plaintiff-bondholders, *may wish* to serve their own



selfish interest. This is an obvious attempt at creating prejudice in this Court against respondents, first by the use of exaggeration, and then building upon it fact-less inference and surmisal. This is all the more meaningless because, as we pointed out, the plaintiffs in the Chancery action will not control that litigation, but the receiver will do so. We thus come back to the Commission's gratuitous assumption that the New Jersey receiver and Chancellor will not adequately protect the rights of all bondholders and other parties—this, despite the pointed statements by this Court in the *Marine Harbor* and *Fidelity* cases that the Commission should not indulge in such speculation.

### CONCLUSION

The writ of certiorari should be denied. It propounds no novel question of bankruptcy law; and the decision below by the Circuit Court, Third Circuit, is not in conflict with the holding of any other circuit courts.

Respectfully submitted,

ROBERT K. BELL,  
Counsel for Respondents.



